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ARCH SPECIALTY INSURANCE COMPANY

**UNITED STATE DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA**

CRAIG MCCRACKEN, an individual  
and LAUREN FAUST, an individual,,

Plaintiff,

v.

ARCH SPECIALTY INSURANCE  
COMPANY, a Nebraska corporation;  
UNITED SPECIALTY INSURANCE  
COMPANY, a Delaware corporation;  
and DOES 1 through 100, inclusive,,

Defendant.

Case No. 2:14-cv-03088-ODW-SH

Judge: Hon. Otis D. Wright, II

**DEFENDANT ARCH SPECIALTY  
INSURANCE COMPANY'S  
MOTION TO DISMISS**

Date: June 2, 2014

Time: 1:30 p.m.

Courtroom: 11

Removed: April 22, 2014

TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

PLEASE TAKE NOTICE that on June 2, 2014 at 1:30 p.m., in Courtroom 11 of the above entitled court, located at 312 North Spring Street, Los Angeles, CA 90012, Defendant ARCH SPECIALTY INSURANCE COMPANY ("Arch") will, and hereby does, move the Court to dismiss the First Amended Complaint ("FAC") against it in its entirety. This motion is brought under Rule 12(b)(6) of the Federal Rules of Civil Procedure on the grounds that Plaintiffs have failed to state a claim for relief since the facts alleged in the FAC, taken together with the terms of the policy issued by Arch as alleged in the FAC, demonstrate that Arch had no duty to defend or indemnify Plaintiffs' assignee, Hess Roofing & Construction, Inc.

1 This motion to dismiss is based on this notice of motion, the memorandum  
2 of points and authorities, the accompanying Request for Judicial Notice, the  
3 pleadings and papers filed in this action thus far, and on any and all further  
4 evidence that may be presented at or before the hearing on this motion.

5  
6 DATED: April 28, 2014

SELMAN BREITMAN LLP

7  
8 By: /S/ GREGORY J. NEWMAN  
9 GREGORY J. NEWMAN  
10 HEE SUNG YOON  
11 Attorneys for Defendant  
12 ARCH SPECIALTY INSURANCE  
13 COMPANY  
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Selman Breitman LLP  
ATTORNEYS AT LAW

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**I. INTRODUCTION<sup>1</sup>**

In 2007, Plaintiffs retained Hess Roofing & Construction, Inc. dba Starlight Construction ("Hess") to replace the roof over parts of their home and install a waterproofing system on their patio deck. Plaintiffs allege that Hess continued working on their home through March 2010. Plaintiffs also allege that their home suffered damage from water intrusion in January 2010. In September 2012, Plaintiffs filed suit against Hess alleging that its work was defective (the "Underlying Action"). Hess allegedly tendered the defense of the Underlying Action to Arch Specialty Insurance Company ("Arch"), who insured Hess under policy number 39CGL04054-00, effective June 5, 2009 to September 22, 2009 (the "Arch Policy"). Plaintiffs thereafter obtained a default judgment against Hess and subsequently received an assignment of Hess's rights under its insurance policies. Plaintiffs then filed the instant action against Arch.

The Arch Policy, like most commercial general liability policies, provides coverage for claims arising out of property damage that occurs *during* the policy period. Here, the property damage alleged by Plaintiffs admittedly occurred *after* the Arch Policy expired. As such, coverage is not triggered under the Arch Policy. Further, the Arch Policy, like most commercial general liability policies, contains exclusions j(5) and j(6), which preclude coverage for damage to property upon which the insured is working. Because Plaintiffs allege that Hess was working on their home from 2007 to 2010, this necessarily encompasses the entirety of the Arch Policy (2009). As such, no coverage would exist for any property damage that may have occurred during the Arch Policy period as a matter of law, *though none is alleged*. Based on the foregoing, Arch had no obligation to defend or indemnify Hess for the Underlying Action and, as a result, has no such obligations

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<sup>1</sup> All factual assertions are taken directly from Plaintiffs' First Amended Complaint, filed in the California Superior Court on January 16, 2014. Plaintiffs' original complaint, filed on December 9, 2013, did not name and was never served on Arch.

1 to Plaintiffs. Without a coverage obligation, there is no basis to support a claim for  
2 breach of the implied covenant of good faith and fair dealing. Therefore, this Court  
3 should grant Arch's Motion to Dismiss, without leave to amend.

## 4 **II. FACTUAL BACKGROUND**

### 5 **A. Allegations in the First Amended Complaint**

6 Plaintiffs Craig McCracken and Lauren Faust are husband and wife and the  
7 owners of real property located at 7270 Mulholland Drive, Los Angeles, California  
8 (the "Property"). First Amended Complaint ("FAC") ¶1. On or about May 2007,  
9 Plaintiffs and Hess entered into a written contract whereby Hess agreed to replace  
10 the built-up roof around the master bedroom and the installation of a waterproofing  
11 deck. FAC ¶10. Hess performed the work until about March 2010, at which time  
12 Hess abandoned the job. *Id.*

13 On or about January 2010, the Property was severely damaged by water  
14 intrusion through the windows, doors, walls and roofs. FAC ¶11. Plaintiffs notified  
15 Hess to make repairs, which Hess refused to do. FAC ¶ 12. Plaintiffs were forced  
16 to hire other contractors and engineers to repair the water damage. *Id.*

17 In September 2012, Plaintiffs filed a complaint in the Los Angeles Superior  
18 Court, alleging causes of action for negligence, negligence per se, breach of  
19 contract, breach of express warranties, and breach of third party beneficiary  
20 contract against Hess and its license bonding company. FAC ¶14. Plaintiffs  
21 obtained a default judgment against Hess. FAC 22. Hess assigned its rights against  
22 its insurers to Plaintiffs. FAC ¶20. The FAC alleges two causes of action for  
23 breach of contract and breach of the implied covenant of good faith.

### 24 **B. The Arch Policy**

25 Arch issued to Hess commercial general liability policy number  
26 39CGL04054-00, effective June 5, 2009 to September 22, 2009 (the "Arch  
27 Policy"). FAC ¶ 2. A certified copy of the Arch Policy is attached hereto as Exhibit  
28 A. As discussed below, the Court can consider the terms of the Arch Policy.

1 The insuring agreement of the Arch Policy states, in pertinent part:

2 1. INSURING AGREEMENT

3 a. We will pay those sums that an insured becomes legally  
 4 obligated to pay as tort damages for bodily injury or  
 5 property damage to which this insurance applies. We  
 6 have the right and duty to defend the insured against any  
 7 suit seeking tort damages provided that no other  
 8 insurance affording a defense against such a suit is  
 9 available to the insured. Our duty to defend the insured  
 10 is further limited as provided below or in the Section of  
 11 the policy entitled "EXCLUSIONS: COVERAGES A  
 12 AND B." We will have no duty to defend any insured  
 13 against any suit seeking damages for bodily injury or  
 14 property damage to which this insurance does not apply.  
 15 We may at our discretion investigate any occurrence and  
 16 settle any claim or suit that may result....

17 b. This insurance applies to bodily injury and property  
 18 damage only if:

19 (1) The bodily injury or property damage is caused by  
 20 an occurrence that takes place in the coverage  
 21 territory; and

22 (2) The bodily injury or property damage is caused by  
 23 an occurrence which takes place during the policy  
 24 period whether or not such occurrence is known to  
 25 any insured; and

26 (3) The bodily injury or property damage resulting  
 27 from such occurrence first takes place during the  
 28 policy period. (See Ex. A at p. A-6.)

23 The Arch Policy contains exclusions that state the insurance does not apply  
 24 to:

25 J. DAMAGE TO PROPERTY EXCLUSION

26 Property damage to:

27 ...



- 1 (5) That particular part of real property on which you or any  
 2 contractors or subcontractors working directly or  
 3 indirectly on your behalf are performing operations, if the  
 4 property damage arises out of those operations; or  
 5 (6) That particular part of any property that must be restored,  
 6 repaired, or replaced because your work was incorrectly  
 7 performed on it.

8 ...  
 9 Paragraph (6) of this Exclusion does not apply to property  
 10 damage included in the products-completed operations hazard.  
 11 (Ex. A at p. A-9 – A-10.)

12 The Arch Policy defines "products-completed operations hazard" as:

13 17. PRODUCTS-COMPLETED OPERATIONS HAZARD

14 Products-Completed operations hazard:

- 15 a. includes all bodily injury and property damage occurring  
 16 away from premises you own or rent and arising out of  
 17 your product or your work except:

- 18 (1) Products that are still in your physical possession;  
 19 or  
 20 (2) Work that has not yet been completed.

- 21 b. Your work will be deemed completed at the earliest of  
 22 the following times:

- 23 (1) When all of the work called for in your contract  
 24 has been completed.  
 25 (2) When all of the work to be done at the job site has  
 26 been completed if your contract calls for work at  
 27 more than one job site.  
 28 (3) When that part of the work done at a job site has  
 been put to its intended use by any person or  
 organization other than another contractor or  
 subcontractor working on the same project.

1  
2 Work that may need service, maintenance, correction,  
3 repair or replacement, after it is complete as set forth in  
4 paragraph b. above, will be treated as completed even  
5 though a contract requires such service, maintenance,  
6 correction, repair or replacement. (Ex. A at p. 21.)

### 7 **III. STANDARDS FOR RULING ON THIS MOTION TO DISMISS**

#### 8 **A. Federal Procedural Standards Apply**

9 Under the Federal Rules of Civil Procedure, a pleading must contain a "short  
10 and plain statement of the claim showing that the pleader is entitled to relief."  
11 Fed.R.Civ.P. 8(a)(2). A court may dismiss an action for failure to state a claim  
12 upon which relief may be granted. *Id.* at 12(b)(6). To survive a motion to dismiss  
13 under Rule 12(b)(6), a complaint must contain sufficient factual matter, accepted  
14 as true, to state a claim to relief that is plausible on its face. *Ashcroft v. Iqbal*, 556  
15 U.S. 662, 678, 129 S.Ct. 1937, 1949 (2009). A motion to dismiss may be granted  
16 based upon an affirmative defense where the complaint's allegations, with all  
17 inferences drawn in plaintiff's favor, nonetheless shows that an affirmative defense  
18 is apparent on the face of the complaint. See *Huynh v. Chase Manhattan Bank*,  
19 465 F.3d 992, 997 (9<sup>th</sup> Cir. 2011) [motion to dismiss was properly granted where  
20 the allegations showed that the claim was barred by the statute of limitations].

21 Further, the court can consider the Arch Policy in ruling on this motion to  
22 dismiss, since documents that are not physically attached to the complaint may be  
23 considered by the court if the complaint refers to such document, the document is  
24 central to plaintiff's claims and no party questions the authenticity of the document.  
25 *United States v. Corinthian Colleges*, 655 F.3d 984, 999 (9<sup>th</sup> Cir. 2011).  
26 "Otherwise, a plaintiff with a legally deficient claim could survive a motion to  
27 dismiss simply by failing to attach a dispositive document on which it relied."  
28 *Pension Benefit Guar. Corp. v. White Consolidated Indus., Inc.*, 998 F.2d 1192,  
1196 (3<sup>rd</sup> Cir. 1993). Indeed, in cases where a plaintiff seeks benefits under an

1 insurance policy, the courts routinely consider the terms and provisions of an  
 2 insurance policy in ruling on a motion to dismiss, even though the policy was not  
 3 attached to the complaint. E.g., *Van Winkle v. Allstate Ins. Co.*, 290 F.Supp.2d  
 4 1158, 1162, fn. 2 (C.D. Cal. 2003); *J & J Pumps, Inc. v. Star Ins. Co.*, 795 F.Supp.  
 5 2d 1023, 1027 (E.D. Cal. 2011). As such, the Court can consider the certified copy  
 6 of the Arch Policy referenced in the FAC (at ¶ 2), which is central to Plaintiffs'  
 7 claims against Arch.

### 8 **B. California Substantive Law Applies**

9 Federal courts exercising diversity jurisdiction must apply the substantive  
 10 state law of the state in which they are located, except on matters governed by the  
 11 U.S. Constitution or federal statutes. *Erie Railroad Co. v. Tompkins*, 304 U.S. 64,  
 12 78, 58 S.Ct. 817, 822 (1938); *Gasperini v. Center for Humanities, Inc.*, 518 U.S.  
 13 415, 427, 116 S.Ct. 2211, 2219 (1996). As the interpretation of contracts is  
 14 considered "substantive," the federal courts must apply state rules. *State of New*  
 15 *York v. Blank*, 27 F.3d 783, 788 (2<sup>nd</sup> Cir. 1994). As such, federal courts in  
 16 diversity cases must apply the state rules for interpretation of insurance policies.  
 17 *Centennial Ins. Co. v. Ryder Truck Rental, Inc.*, 149 F.3d 378, 381 (5<sup>th</sup> Cir. 1998).

18 When undertaking this task, a federal court sitting in diversity is to  
 19 approximate state law as closely as possible. In doing so, federal courts are bound  
 20 by the pronouncements of the state's highest courts on applicable state law.  
 21 *Ticknor v. Choice Hotels Intern., Inc.*, 265 F.3d 931, 939 (9th Cir. 2001). When  
 22 the state's highest court has not decided an issue, the task of the federal courts is to  
 23 predict how a state high court would resolve it. *Id.* If there is relevant authority  
 24 from the state's intermediate appellate court, the federal court must follow the  
 25 state's intermediate appellate court, unless the federal court finds convincing  
 26 evidence that the state's highest court would not follow it. *Chalk v. T-Mobile USA,*  
 27 *Inc.*, 560 F.3d 1087, 1092 (9th Cir. 2009).

28 Without question, California law governs the interpretation of the Arch

1 Policies. As such, this court must look to relevant California authority when  
2 interpreting the provisions of the Arch Policies, including pronouncements of the  
3 California Courts of Appeals that have interpreted similar provisions.

4 **IV. PLAINTIFFS' FIRST AMENDED COMPLAINT ALLEGES FACTS**  
5 **PROVING THAT NO COVERAGE EXISTS UNDER THE ARCH**  
6 **POLICY AS A MATTER OF LAW**

7 **A. The First Amended Complaint Only Alleges Property Damage**  
8 **That Occurred *After* the Arch Policy Expired**

9 The Arch Policy only provides coverage for bodily injury or property  
10 damage is caused by an occurrence that takes place during the policy period. Ex.  
11 A at p. A-6, Insuring Agreement ¶b(2). Under California law, it is well settled that  
12 the time of occurrence of an accident is the time when the complaining party was  
13 actually damaged, not the time the wrongful act was committed. *Hallmark Ins. v.*  
14 *Sup. Ct.*, 201 Cal.App.3d 1014, 1017 (1988). The time of occurrence of an accident  
15 refers to the event causing the actual injury, and not an earlier event which caused  
16 the potential for future injury. *Id.* at 1018. Here, the policy ended on September  
17 22, 2009 and the "property damage" did not occur until January 2010. As such, the  
18 requirement for coverage to exist under ¶b(2) is not satisfied.

19 Further, the Arch Policy only provides coverage for bodily injury or  
20 property damage that first takes place during the policy period. Ex. A at p. A-6,  
21 Insuring Agreement ¶b(3). Again, the only "property damage" alleged in the FAC  
22 is alleged to have occurred in January 2010 (FAC ¶ 11), which is after the Arch  
23 Policy expired. FAC ¶ 2. Indeed, the Policy was cancelled on September 22, 2009.  
24 Ex. A, p. A-37. As such, the requirement for coverage to exist under ¶b(3) is not  
25 satisfied. See *Whittaker Corp. v. Allianz Underwriters, Inc.*, 11 Cal.App.4<sup>th</sup> 1236,  
26 1243 (1992) [a policy is triggered when the time of the injury is within the  
27 effective dates of the policy].

28 Based on the foregoing, there is no possibility of coverage under the Arch

1 Policy as a matter of law. As such, Arch had no obligation to defend or indemnify  
2 Hess for the Underlying Action and, as a result, no such obligations to Plaintiffs.

3 **B. Exclusions J(5) and J(6) Preclude Coverage For Any Property**  
4 **Damage That May Have Occurred While Hess Was Performing Work**  
5 **on Plaintiffs' Home, Though No Such Property Damage Was Alleged**

6 The Arch Policy also contains exclusion j(5), which precludes coverage for  
7 "property damage" to that particular part of real property upon which the named  
8 insured is performing operations, if the property damage arises out of those  
9 operations. Ex. A at p. A-9 – A-10. Further, exclusion j(6) precludes coverage for  
10 the repair or replacement of that particular part of any property upon which the  
11 named insured performed work, to the extent that the "property damage" was the  
12 result of the named insured's faulty workmanship on that part of the work, and, to  
13 the extent that said "property damage" is not included in the "products-completed  
14 operations hazard." *Id.* In *Baroco West, Inc. v. Scottsdale Ins. Co.*, 110 Cal.App.4th  
15 96 (2003), a general contractor began construction work during the policy period  
16 but did not complete his work until after the policy expired. The court held that the  
17 policy did not provide coverage since exclusions j(5) and j(6) precluded coverage  
18 for any property damage caused during ongoing construction activities. *Id.* at 103-  
19 104.

20 The applicability of exclusions j(5) and j(6) was reinforced in *Clarendon*  
21 *America Ins. Co. v. General Sec. Indem. Co. of Arizona*, 193 Cal.App.4th 1311  
22 (2011). In this regard, the court stated, at 1325-1326:

23 The exclusion found in j(5) applies to work in progress. The insurer is  
24 not obligated to indemnify a policyholder for property damage that  
25 occurs while the insured is performing operations on that property.  
26 Thus, if the [Claimants'] claims encompassed property damage that  
27 occurred while [the insured] or its subcontractors were performing  
28 operations on the property, no coverage would exist.

1 The exclusion found in j(6) excludes coverage for the physical injury  
 2 to, or loss of use of, that part of the property that must be replaced  
 3 because [the insured's] work was performed incorrectly. This  
 4 precludes coverage for the claims asserted by the [Claimants] against  
 [the insured], which were based on alleged "defects and deficiencies"  
 in the residence resulting from poor workmanship and/or materials.

6 Here, the FAC alleges that Hess began its work on Plaintiffs' home in 2007  
 7 (FAC ¶10) and "continued to work at the Real Property through March 2010,  
 8 including work that caused water damage on or about January 2010." FAC ¶17.  
 9 Since the Plaintiffs allege that Hess did not complete its work as of March 2010,  
 10 this necessarily means Hess was performing operations at Plaintiffs' home during  
 11 the pendency of the Arch Policy, from June 5, 2009 to September 22, 2009. As  
 12 such, exclusions j(5) and j(6) would preclude coverage for any property damage  
 13 that may have occurred while Hess was working on Plaintiffs' home, though none  
 14 was alleged.

15 **C. Arch Cannot Be Liable for Breach of the Implied Covenant As A**  
 16 **Matter of Law**

17 As stated by the California Supreme Court, "if there is no potential for  
 18 coverage, and hence no duty to defend under the terms of the policy, there can be  
 19 no action for breach of the implied covenant of good faith and fair dealing."  
 20 *Waller v. Truck Ins. Exch. Inc.*, 11 Cal.4<sup>th</sup> 1, 35 (1995). Since there was no  
 21 possibility of coverage under the Arch Policy for the Underlying Action, Arch  
 22 cannot be liable for breach of the implied covenant of good faith and fair dealing.

23 **V. THE COURT SHOULD GRANT ARCH'S MOTION TO DISMISS**  
 24 **WITHOUT LEAVE TO AMEND**

25 If a complaint is dismissed for failure to state a claim, leave to amend may  
 26 be denied if amendment would be futile. *Albrecht v. Lund*, 845 F.2d 193, 195-196  
 27 (9<sup>th</sup> Cir. 1988). In determining whether amendment would be futile, a court should  
 28 examine whether the complaint can be amended to cure the defect "without



contradicting any of the allegations of the [operative] complaint." *Reddy v. Litton Industries, Inc.*, 912 F.2d 291, 296-297. While leave to amend is often liberally granted, the amended complaint can only allege other facts that are *consistent* with those in the challenged pleading. *Id.* Here, Plaintiffs cannot cure the defects in its FAC without contradicting the allegations regarding when the property damage occurred, when Hess completed its work or the effective period of the Arch Policy. As such, this Court should grant this motion to dismiss without leave to amend.

## VI. CONCLUSION

As demonstrated above, Plaintiffs' allege the very facts that preclude coverage for the Underlying Action under the Arch Policy as a matter of law. That the damages occurred after the Arch Policy expired is alone enough for the Court to grant the motion to dismiss. However, Plaintiffs also alleged that Hess was working on their home during the entirety of the Arch Policy period, and the Arch Policy precludes coverage for any damage that occurs while Hess was working on their home (again, though no such property damage was alleged). As such, Arch had no duty to defend or indemnify Hess the Underlying Action and, as a result, cannot be liable for breach of the implied covenant of good faith as a matter of law. Therefore, Plaintiffs, as assignees of Hess, are not entitled to any relief under the Arch Policy.

Based on the foregoing, Arch respectfully requests that this Court grant its motion to dismiss without leave to amend, since no amendment can bring Plaintiffs' claim within the coverage of the Arch Policy.

DATED: April 28, 2014

SELMAN BREITMAN LLP

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